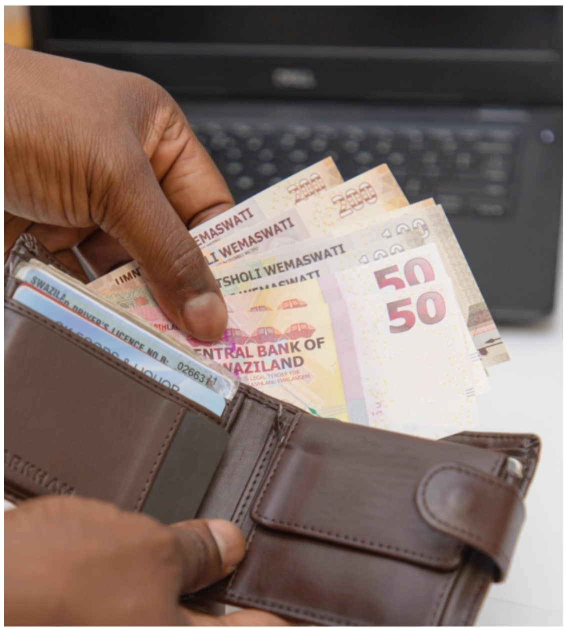
Umntsholi News

CENTRAL BANK OF ESWATINI
Umntsholi Wemaswati

...with your Hostess Lindokuhle Sithole, Senior Communication and International Relations Officer

Indebtedness



Being indebted, at some point in life, is inevitable. However, what becomes problematic is when taking up debt leads to over-indebtedness. There is an economic and socio-psychological impact to individuals that find themselves over-indebted.

From an economic perspective, over-indebted consumers often face liquidity constraints because they are unable to borrow against future earnings, making it increasingly challenging to meet their financial needs. On the socio-psychological front, individuals with unmet debt obligations are at a higher risk of depression than those without financial difficulties. Unsettled financial obligations have also been associated with poor health patterns, including physical illness.

Over-indebtedness is therefore a concern to the Central Bank as it can have adverse repercussions to the attainment of its goal of financial stability and overall economic development in Eswatini, in addition to the adverse impact it has on the financial consumer's well-being.

This article discusses the drivers, signs, and symptoms of over-indebtedness, how it could be avoided. It also seeks to recommend what one could do if they are already highly indebted.

What is Over-indebtedness?

While there is no universal definition of over-indebtedness. Most definitions broadly converge on the following aspects: making high repayments relative to income, being in arrears, making heavy use of credit, and finding debt a burden. According to the eSwatini Consumer Credit Act (CCA), 2016 (as amended), a consumer is over-indebted when the gravity of available information at the time a determination is made indicates that the consumer is, or will be, unable to satisfy in a timely manner, all the obligations under all the credit agreements to which the consumer is a party.

Signs Indicating that you are Over-indebted

The following are some signs of over-indebtedness:

1. High debt to income ratio

In Eswatini, the prescribed debt to income ratio is 33%. If your debt obligations are consistently above this threshold against your income, then this is a sign of a financial strain.

2. Late payment and default (arrears)

Repeated late payment of standing loan obligations is another indicator that a consumer is experiencing a significant financial burden. This situation is further worsened in that consumers under default then incur penalty fees, and a host of other fees like attorney's fees.

3. Continuous borrowing/ taking multiple loans

If you find yourself taking one loan after another or taking up a loan from one financial services provider for the purpose of settling a debt with another service provider, that points to your inability to honor your financial obligations. Additionally, the more you borrow, the more you will have to pay back every month.

4. When debt becomes a burden

We often hear of people complaining about not seeing the value of being employed because a large portion of their salary is consumed by multiple bank stop orders. There have sadly been incidents of suicide due to failure to handle the stress and anxiety that comes with debt. Stress affects emotional, physical, cognitive, and behavioral wellness and can have an obvious impact on your quality of your life and the people around you.

What Causes Over-indebtedness and How this can be avoided

1. Over-spending

In most cases consumers do not follow the recommended “50-30-20” budgeting principle which advocates for allocation of 50% of income towards basic needs: food, transport/mortgage/rent, 30% towards non-basic, everyday expenses like leisure activities and 20% towards savings. As a consumer, it is important that you create a budget and consistently monitor your financial affairs to keep track of your expenditure daily.

2. Reckless Credit by FSPs

Reckless credit by Financial Services Providers (FSPs) including banks can also be a cause for consumer over-indebtedness. Section 26 of the CCA requires FSPs to assess a consumer's financial affordability to inform the decision whether to grant or refuse a loan or credit. Therefore, based on this assessment, the FSP should be able to determine if a consumer is overly committed by looking at the customer's financial obligations.

Section 25(1) of the CCA states that the consumer shall fully and truthfully answer any requests for information by the financial institution when applying for new loans. Therefore, consumers also have a role to play by providing all the relevant information including all their standing financial commitments not only from formal FSPs but also with informal money lenders like stokvels and loan sharks. Consumers are urged to stop the adverse practice of going to different FSPs to initiate new loans when one of their loans is cleared or their income increases.

What to do if you are already highly indebted?

The CCA under Section 86 gives a right to the consumer to apply to a debt counsellor so that an assessment can be made as to whether he/she is over-indebted. Should this assessment reveal that the consumer is over-indebted, negotiation can then be made between the consumer and the credit provider to come up with a debt rearrangement plan. If there is no agreement, the debt counsellor could make an application to a court of law, on behalf of the consumer, so that one or more of the consumer's debts can be re-arranged or declared reckless credit. Below are other suggestions on how you can get out of over-indebtedness.

1. Do not take on more debt

Cut back on, or stop using credit cards, and loans to cover expenses as much as possible to avoid accumulating new debts.

2. Cut out unnecessary expenses

Since you need to reduce your payment obligations, review your spending, and eliminate or reduce some non-essential expenses (even temporarily) until your finances are in order.

3. Make a payment plan

Create a schedule based on your income and the due dates of your payment obligations so that you know what you are paying for each month and can then adjust your expenses or start a side hustle to top up your income, where possible. This adds more payments and clears your debts quicker.

Conclusion

We all have a role to play in curbing over-indebtedness. This includes FSPs, banks, regulators, and consumers. FSPs should be prudent and refrain from seeking quick gains in market share but embrace a more rigorous credit discipline as the foundation for sustainable growth. Consumers should provide all necessary information and avoid overspending and incurring unnecessary debt.

The Central Bank plays its part in ensuring that FSPs comply with set regulatory requirements in addition to other initiatives to empower financial services consumers so that they can make sound financial decisions.

The Bank also continues to work with other stakeholders in initiatives aimed at ensuring that valuable information on consumers is readily available to drive financial literacy. For example, the development of a national credit registry and regulations governing credit bureaus like ITC so that there be a consolidated record on all credit provided in the country which can give consolidated view of the actual debt that a consumer has across all FSPs, also giving a true picture on the overall actual level of household indebtedness in the country.